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Province Of Alberta Review of Financial
Position As At September 30, 1971. 2



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PROVINCE OF ALBERTA

REVIEW OF FINANCIAL POSITION

AS AT SEPTEMBER 30, 1971

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February 22, 1972

The Honourable G. T. W. Miniely
Provincial Treasurer
Province of Alberta
Edmonton, Alberta

Sir:

As requested, we have reviewed the financial position of the Province of Alberta including an assessment of the realizable value of assets and their related liquidity. Our study did not include an audit of the accounts of the Province but rather consisted of a review of the audited financial statements contained in the Public Accounts as at March 31, 1971, together with an evaluation of the investments and capital loans and advances of the Province as at September 30, 1971. Projections of the financial position of the Province at March 31, 1972 are as estimated by the Provincial Auditor and are based on the actual results for the nine months to December 31, 1971 and an estimate of the three months to March 31, 1972.

We have completed our review and are submitting our report on the liquidity position and the financial position of the Province.

We wish to express our appreciation of the excellent co-operation we received from the Provincial Auditor and from employees of the government and of the government agencies visited during our review.

Yours very truly,

Touche Ross & Co.

Chartered Accountants

PROVINCE OF ALBERTA

REVIEW OF FINANCIAL POSITION

AS AT SEPTEMBER 30, 1971

PROVINCE OF ALBERTA

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PROVINCE OF ALBERTA

LIQUIDITY POSITION OF THE PROVINCE

During the years when the Province was accumulating surpluses, the funds were invested in securities or used to finance long-term capital loans and advances; at March 31, 1970, \$403 million of surplus funds had been invested in this manner.

The nature of the investments and loans was such that they could not be readily converted to cash and accordingly, in the past two years, the Province has had to draw on its cash balances and resort to borrowings to finance its deficits.

To illustrate this situation, we have prepared the following summary from audited financial statements appearing in the Public Accounts and from unaudited pro-forma financial statements prepared by the Provincial Auditor:

	<u>Audited Statements</u>		<u>Pro-forma Statements</u>	
	<u>March 31</u> <u>1970</u>	<u>March 31</u> <u>1971</u>	<u>Sept. 30</u> <u>1971</u>	<u>March 31</u> <u>1972</u>
	(000 omitted)			
Loans and advances	\$231,900	\$221,100	\$213,100	\$225,700
Investments	<u>171,100</u>	<u>151,200</u>	<u>148,600</u>	<u>142,500</u>
	403,000	372,300	361,700	368,200
Cash	155,000	143,300	20,500	94,900
Other assets	<u>90,000</u>	<u>96,100</u>	<u>98,700</u>	<u>96,100</u>
	648,000	611,700	480,900	559,200
Less:				
Payables & accruals	<u>43,100</u>	<u>41,100</u>	<u>41,100</u>	<u>42,400</u>
	604,900	570,600	439,800	516,800
Funded debt	<u>37,300</u>	<u>105,300</u>	<u>154,800</u>	<u>202,000</u>
Net Assets (1)	<u>\$567,600</u>	<u>\$465,300</u>	<u>\$285,000</u>	<u>\$314,800</u>

(1) Subject to provisions for losses on realization as set out later in this report.

At March 31, 1971, the Province had \$143.3 million cash on hand which was insufficient to meet obligations expected to become due in the next six months. For this reason, the Province borrowed \$50 million in June 1971 through an issue of long-term debentures.

At September 30, 1971, the Province's cash balances had been reduced to approximately \$20.5 million. The remaining assets of the Province consisted mainly of investments, loans and advances. Our comments on the liquidity of these assets as at September 30, 1971 are as follows:

1) Investments

The position of the Special Investment Fund at September 30, 1971 was as follows:

	<u>Book Value</u>	<u>Approximate Market Value</u>
	(000 omitted)	
Government of Canada, direct and guaranteed	\$ 52,000	\$ 47,000
Provincial, direct and guaranteed	55,800	50,600
Municipal	19,800	17,300
Municipal hospital districts	1,400	1,000
School districts and divisions	<u>19,600</u>	<u>14,800</u>
	<u>\$ 148,600</u>	<u>\$ 130,700</u>

(Approximate average yield 4.6%)

The Province will realize approximately \$6.1 million prior to March 31, 1972 and \$6.8 million in each of the next three years upon maturity of securities presently held in the Special Investment Fund. Apart from the Government of Canada bonds and \$14 million of the Provincial direct and guaranteed debentures, these securities are not readily marketable and will probably have to be held to maturity. In the case of the Government of Canada bonds and the marketable Provincial direct and guaranteed debentures, any sales would result in losses to the Province.

2) Loans and advances

These loans and advances are mainly of a long-term nature. Annual repayments are estimated to be approximately \$13 million in each of the next three years but these will not ease the liquidity position of the Province if new loans exceed the annual repayments as is expected to be the case in the current fiscal year.

3) Other assets

The other assets of the Province consist of inventories, equipment, working advances, prepaid expenses, accrued interest, and accounts receivable. Such assets are necessary for the normal operations of the Province and there is little opportunity to reduce the amount of funds committed to these assets.

The cash balances of \$20.5 million at September 30, 1971 were insufficient as of that date to meet current obligations. In order to be in a liquid position, the Province had the alternative of either realizing on certain of its assets or resorting to additional long-term borrowings. As indicated above, the only assets which could readily be converted to cash were certain of the investments having a book value of \$66 million but the sale of these investments would have resulted in a loss to the Province of approximately \$6 million. Rather than sustain these losses, the Province issued \$50 million of debentures in October 1971 to maintain its liquid position through the balance of the fiscal year.

Government revenues and expenditures do not flow evenly throughout the year. During the current fiscal year expenditures, as was anticipated, have been greatest during the period April 1 - December 31, while revenues are expected to exceed expenditures during the period January 1 - March 31. The cash position is therefore expected to improve during the remainder of the current fiscal year ending March 31, 1972.

Summary

The liquid assets of the Province as at September 30, 1971 consisted of \$20.5 million cash and marketable securities having a realizable value of approximately \$60 million. Rather than liquidating these investments with the resultant loss of \$6 million, an additional \$50 million of debentures were issued in October 1971 to meet cash requirements of the Province for the remainder of the year.

PROVINCE OF ALBERTA

FINANCIAL POSITION OF THE PROVINCE

At March 31, 1971 the surpluses and reserves of the Province as shown on the audited financial statements totalled \$456.5 million. The latest estimates prepared by the Provincial Auditor, based on actual expenditures for the nine months to December 31, 1971, indicate that the deficit for the current fiscal year will be approximately \$150.6 million. Based on the past practices followed by the Province, it is now anticipated that the surpluses and reserves will be reduced to \$305.9 million at March 31, 1972.

Practices of provincial governments vary widely in the reporting of their operations, particularly when these operations are carried out through Crown enterprises, commissions and agencies. The balance sheet of a province reflects the method which it has used in financing these operations.

The Province of Alberta (with certain exceptions, principally the Alberta Liquor Control Board) does not include the accounts of government enterprises, commissions and agencies in its consolidated balance sheet except to the extent of advances made to such bodies. When these enterprises, commissions or agencies borrow funds which are guaranteed by the Province, the amounts are shown as contingent liabilities in a note to the consolidated balance sheet.

In our opinion, debentures of provincial commissions and agencies which have no offsetting realizable assets and which are entirely dependent upon contributions from the province to cover debt charges, should be added to the debt of a province in order to assess its financial position. In the case of the Province of Alberta, these would include debentures of the following:

The Alberta Universities Commission

Certain capital grants to universities were financed by the Commission through the issuance of debentures guaranteed by the Province of Alberta. The outstanding debentures, less sinking funds, total approximately \$41.5 million and are shown as contingent liabilities on the balance sheet of the Province. The Province is directly liable for the repayment of these debentures and for the annual interest payments.

Provincially Owned Hospitals

Outstanding debentures of Foothills Provincial Hospital, Glenrose Provincial General Hospital and University of Alberta Hospital total approximately \$22 million at December 31, 1971. The Province provides the funds to cover interest and capital repayments under the Hospitalization Benefits Plan.

Normally the accounts of government enterprises are only included in the statements of a government to the extent of investments in and advances to such enterprises. In the case of the Province of Alberta, however, we consider that the Alberta Resources Railway Corporation should be taken into account in assessing the overall financial position of the Province.

Alberta Resources Railway Corporation

The railway was constructed at a capital cost of approximately \$110 million, including the capitalization of interest during the period of construction. The railway was financed through an issue, by the railway itself, of short-term debentures totalling \$95 million and guaranteed by the Province of Alberta. The \$95 million in short-term debentures are scheduled to come due in the next three years. Since there is no likelihood that the railway will be able to meet these obligations as they become due, it will be necessary for the railway to issue new debentures or for the Province to provide funds for the redemptions.

Revenues obtained from railroad operations are, at present, insufficient to meet operating costs including interest on the debentures. As a result, the Province has had to advance funds to cover the operating deficits and we have made provision for possible losses on recovery of the advances made to date.

Canadian National Railways has undertaken to operate the railway under a long-term agreement with an option to purchase. It is our opinion that, unless there is a substantial improvement in operating results, Canadian National Railways will not find it economically feasible to exercise their option to purchase the railway.

Since this investment is not a self-supporting asset and, in our opinion will not be in the foreseeable future, the debentures should be shown as direct debt of the Province in assessing the Province's financial position.

It has not been the practice of the Province to reduce its loans and advances to estimated realizable values nor to provide in its accounts for possible losses on implementation of guarantees. In our opinion, based on our review of the outstanding loans and guarantees, a provision of \$43.9 million is required for this purpose.

The following is a summary of the adjustments which, in our opinion, are required to arrive at the overall financial position of the Province:

(000 omitted)

Provisions to reduce capital loans and advances to estimated realizable values	
Alberta Health Plan	\$ 9,800
Alberta Resources Railway Corporation	4,600
Other	<u>6,200</u>
	20,600
Provision for possible loss on accounts and interest receivable from Alberta Resources Railway Corporation	19,500
Provision for possible losses on guaranteed loans	<u>3,800</u>
	43,900
Guaranteed debt of The Alberta Universities Commission	\$ 41,500
Debt of Provincially Owned Hospitals	22,000
Guaranteed debt of Alberta Resources Railway Corporation	<u>95,000</u>
	<u>158,500</u>
	<u>\$ 202,400</u>

The effect of these adjustments on the pro-forma consolidated balance sheet of the Province of Alberta as at March 31, 1972 is as follows:

PROVINCE OF ALBERTA

CONDENSED CONSOLIDATED BALANCE SHEET AND
PRO-FORMA CONSOLIDATED BALANCE SHEETS

(000 omitted)

	<u>Public Accounts</u>	<u>Pro-forma</u>	<u>Pro-forma</u>
	<u>March 31, 1971</u>	<u>March 31, 1972</u>	<u>March 31, 1972</u>
		(1)	(2)
Loans and advances	\$ 221.1	\$ 225.7	\$ 205.1
Investments (3)	<u>151.2</u>	<u>142.5</u>	<u>142.5</u>
	372.3	368.2	347.6
Cash	143.3	94.9	94.9
Other assets	<u>96.1</u>	<u>96.1</u>	<u>76.6</u>
	\$ 611.7	\$ 559.2	\$ 519.1
	<u>=====</u>	<u>=====</u>	<u>=====</u>
Funded debt	\$ 105.3	\$ 202.0	\$ 360.5
Payables and accruals	41.1	42.4	46.2
Unearned revenue	<u>8.8</u>	<u>8.9</u>	<u>8.9</u>
	155.2	253.3	415.6
Surplus and reserves	<u>456.5</u>	<u>305.9</u>	<u>103.5</u>
	\$ 611.7	\$ 559.2	\$ 519.1
	<u>=====</u>	<u>=====</u>	<u>=====</u>

- (1) Projections estimated by Provincial Auditor based on actual results for the nine months to December 31, 1971 and an estimate of the three months to March 31, 1972.
- (2) Adjusted for items referred to in Touche Ross assessment of financial position.
- (3) Does not include any adjustment of securities to market values since, as noted earlier in this report, most of these securities will, in all likelihood, be held to maturity.

Summary

The condensed pro-forma consolidated balance sheet as at March 31, 1972 shows funded debt of \$360.5 million as compared to \$202 million before adjustment and shows surplus and reserves of \$103.5 million compared to \$305.9 million before adjustment.

The funded debt of \$360.5 million represents the debt of the Province and of its enterprises, commissions and agencies which must be supported out of the general funds of the Province.

The decrease in surplus and reserves of \$202.4 million results from the provisions which, in our opinion, are required to provide for estimated losses on loans and guarantees and from the adjustments required to give effect to our recommended treatment of the debts of certain Crown enterprises and agencies in assessing the overall financial position of the Province. In the case of the Alberta Universities Commission and the Provincially owned hospitals, the adjustments to surplus conform with the treatment which would have been given these items had the debt been incurred directly by the Province. In the case of the Alberta Resources Railway Corporation, the adjustment to surplus represents the provision which would be required to reduce the investment in the railroad to a nominal value since, in our opinion, this should not be considered a realizable asset; the effect of this adjustment is to treat the railroad in the same manner as other capital assets of the Province such as bridges and highways.

PROVINCE OF ALBERTA

CONTINGENT LIABILITIES AND COMMITMENTS
AS AT SEPTEMBER 30, 1971

Contingent liabilities of the Province at September 30, 1971
were as follows:

(000 omitted)

Guaranteed debentures	
Alberta Municipal Financing Corporation	\$ 857,000
Alberta Government Telephones	402,800
Alberta Housing Corporation	13,200
Other	<u>1,100</u>
	1,274,100
Guaranteed bank loans	27,300
Other guarantees	<u>18,700</u>
Total Contingent Liabilities	<u>\$ 1,320,100</u>

The above contingent liabilities do not include the undernoted
guaranteed debentures which we have included with direct debt of the Province
in our assessment of the overall financial position:

Alberta Resources Railway Corporation	\$ 95,000
The Alberta Universities Commission	41,000

In our opinion, an amount of \$3.8 million is required to provide
for possible losses on guaranteed bank loans.

The Province was, at September 30, 1971, committed to the expenditure
of funds in future years in connection with the undernoted items:

Debt of \$85 million of hospitals not provincially owned.
While the Province has not committed itself to the repayment of this
debt, the payment of principal and interest presently comes out of
funds received from the government through the Hospitalization Benefits
Plan.

Matching contributions to the Three Alberta Universities Capital Fund Committee up to a maximum of \$25 million except to the extent of \$5.3 million provided for in the estimated deficit for the year ending March 31, 1972.

Capital grants to colleges and universities to cover the completion of approved projects in the amount of approximately \$31 million.

Estimated cost of completing Highways Department contracts.

These commitments do not include statutory obligations such as interest on debentures nor do they include the following commitments, the amount of which cannot be determined at this time:

Pensions under provision of The Public Service Pension Act, The Local Authorities Pension Act and the M.L.A. Pension Act. Contributions received are currently credited to the General Revenue Fund of the Province and payments required under the Acts are made through appropriations therefrom. An actuarial survey is required to determine the Province's liability under the Acts.

Liabilities, if any, in connection with the liquidation of Security Trust Company.

